

BEFORE THE
POSTAL REGULATORY COMMISSION
WASHINGTON, DC 20268-0001

PHI ACQUISITIONS NSA

Docket No. MC2014-21

PHI ACQUISITIONS NSA

Docket No. R2014-6

**RESPONSES OF THE UNITED STATES POSTAL SERVICE TO
CHAIRMAN'S INFORMATION REQUEST NO. 3**

(April 16, 2014)

The United States Postal Service hereby provides its responses to Chairman's Information Request (CHIR) No. 3, issued April 11, 2014. Responses were due by April 16, 2014. Each question is reprinted verbatim in the attached, and is followed by the Postal Service's response.

Respectfully submitted,

UNITED STATES POSTAL SERVICE

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April 16, 2014

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1. Please refer to "Panzar_PHI_With_Exigency.xlsx", workbook tab "MC2004-3 Analysis".
 - a. Please confirm that the marginal discount in Cell E11 should be \$0.049 ($0.243 * 0.20 = 0.049$). If not confirmed, please explain.
 - b. Please confirm that the Enhanced Carrier Route (ECR) Flats rebate paid in Cell E14 should be \$1,198,169 as shown in "PHI_NSA_Financials FINAL_Exigent.xlsx", workbook tab "4_Tier," Cell C32. If not confirmed, please explain.
 - c. If part (a) and/or part (b) are confirmed, please provide revised workpapers.

RESPONSE:

- a. Confirmed.
- b. Confirmed.
- c. Revised workpapers are attached as "Panzar_CHIR3Q1.xlsx".

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2. Please refer to "PHI_NSA_Financials.FINAL.xlsx", filed with the Notice, and "PHI_NSA_Financials FINAL_Exigent.xlsx", which incorporates the reduced Annual Volume Threshold resulting from the exigent rates that went into effect on January 26, 2014. The forecasts for the Before Rates Volume for Year 1 through Year 5 in workbook tab "1_Inputs", Cells H174 through L174, and the NSA volume forecasts for Year 1 through Year 5 of the contract in workbook tab "1_Inputs", Cells D200 through H200 in "PHI_NSA_Financials FINAL_Exigent.xlsx" are lower than the corresponding figures in "PHI_NSA_Financials.FINAL.xlsx".
 - a. Please provide an explanation for the decrease in before rates volumes and NSA volumes forecasted.
 - b. Please provide the calculation of the adjustments to the before rates volumes and the NSA volumes forecasted.

RESPONSE:

- a. The before rates volumes and the NSA volumes forecasted were decreased because those volumes would be reduced due to the increased exigency postage. To derive the new before rates volumes and NSA volume forecasts, the same logic used to develop the exigency-adjusted Annual Volume Threshold was applied. The methodology is spelled out in Section III.D. of the NSA, which provides for adjustment to the Annual Volume Threshold in the event of a postal rate increase resulting in an increase to PHI's Total Annual Postage of more than 20 basis points. The threshold adjustments were designed to account for the likely effect of such an increase on PHI's mail volume. It is logical to apply the same adjustment to the before-rates volumes and NSA volume forecasts, as PHI would be expected to mail less at the higher exigent rates.

As detailed in the response to Question 2(b) and the workpapers accompanying the response to Question 3, the adjustment percentage of 6.67 percent was derived by

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determining the actual postage increase PHI would have experienced on its mail volume for the four quarters prior to the increase, determining the percentage increase this reflects (minus the change in CPI-U), and adjusting this figure by a factor of 1.4. As explained in the response to CHIR No. 1, Question 11(a), the adjustment factor was based on the behavioral characteristics of PHI's internal models and business practices, as well as the methodology used by PHI to plan mail volume, which uses variable costs such as postage to make economic decisions on how deeply to mail rank-ordered cells, lists, or household segments. It reflects the fact that as postage rates increase, it becomes less economically viable for PHI to mail to certain prospect lists or household segments.

b. The before rates volumes and the NSA forecasted volumes are both decreased from the prior volumes by 6.67 percent. The before rates volumes are rounded to the nearest thousand and the NSA forecasted volumes are rounded to the nearest million. The 6.67 percent is the calculated Baseline and Annual Threshold adjustment due to exigency. Please also see the response to Question 3.

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3. Please refer to "PHI_NSA_Financials.FINAL.xlsx", filed with the Notice, and "PHI_NSA_Financials FINAL_Exigent.xlsx", which incorporates the reduced Annual Volume Threshold resulting from the exigent rates that went into effect on January 26, 2014.
 - a. Please provide the billing determinants for PHI Eligible Mail used to calculate the Total Annual Postage increase percentage. See section III.D. of the Agreement.)
 - b. Please provide workpapers detailing how the Total Annual Postage increase percentage was used to calculate the adjusted thresholds.

RESPONSE:

a-b. The postage factors used and the calculation of the Total Annual Postage increase percent and the resulting baseline adjustments are shown in detail in "ExigencyAdj_CHIR3Q3.xlsx", attached. Note that this analysis was done jointly with PHI and the vendor (QuadGraphics) that produces the tier qualified mail files for PHI. Noting that the exigency rates impact total postage costs differently on mail streams of different volumes which have a different mix of work-share discounts, and following the approach defined in the Agreement, the analysis used actual PHI mail events from 2013 of representative volumes and re-processed them with the new exigency postal rates, calculated the increase in postage, applied that increase to the annual mail streams of comparable sizes, then calculated the average increase due to exigency. The Postal Service audited the data and the process. The data files supplied have been edited to remove company confidential information such as mail dates and brand names.

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4. In "PHI_NSA_Financials_FINAL_Exigent.xlsx," workbook tab "3_Revenue and Cost," Cells F16 through F18, the Postal Service adjusted the price per piece by 4.3 percent to reflect the exigent rates that went into effect on January 26, 2014.

- a. Please explain how the exigent price increase multiplier of 4.3 percent was derived.
- b. Please confirm that the price increase used in the calculation of the adjustment to the threshold should also be 4.3 percent, consistent with the adjustment to the price per piece. If not confirmed, please explain.

RESPONSE:

a. 4.3 percent is the average exigent price increase for Standard Mail Flats implemented in January 2014. This percentage was used as a practical estimate of the exigent price increase multiplier in the NSA.

b. Not confirmed. The price increase used in the calculation of the adjustment of the threshold is defined in Section III.D of the NSA. See the detailed analysis and calculation of the exigency adjustment in response to Question 3.